In the United States Bankruptcy Court
for the
Southern District of Georgia
Savannah Division

In the matter of:)
)
SAVANNAH YACHT CORPORATION)
)
Debtor)

Chapter 7 Case

Number 03-41547

MEMORANDUM AND ORDER
DENYING RULE 2004 EXAMINATION OF DEBTOR
AND GRANTING MOTION TO DISMISS

M. H. Yacht Sales, Inc. ("M. H. Yacht"), as sole petitioning creditor, filed an Involuntary Chapter 7 Petition against Savannah Yacht Corp. ("Debtor") on May 16, 2003. Jay Ecklund ("Ecklund") filed a Motion for Bankruptcy Rule 2004 Examination of Debtor on August 12, 2003. Subsequently, M. H. Yacht. filed a Motion to Dismiss Involuntary Petition With Consent of Debtor on December 22, 2003. A hearing regarding the motions of M.H Yacht and Ecklund was held on January 26, 2004. This matter is a core proceeding within the jurisdiction of this Court under 28 U.S.C. § 157(b). Pursuant to Federal Rule of Bankruptcy Procedure 7052(a), I make the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

On June 11, 2003, Ecklund filed a Motion to Modify Automatic Stay in

order to resolve a pre-petition contractual dispute through arbitration. Prior to the involuntary petition being filed, Debtor had filed a demand for arbitration following which Debtor and Ecklund had chosen an arbitration panel and begun the process that would culminate in a hearing before that panel. In the arbitration, Debtor contended that Ecklund owed it $420,400.00 for work done by Debtor pursuant to a contract on Ecklund's vessel, the M/Y Starlight. In contrast, Ecklund asserted in the arbitration proceeding that Debtor breached its contract by, among other things, failing to proceed under the contract in a timely manner and complete the work on his vessel. This Court entered a consent order on July 18, 2003, allowing Ecklund and Debtor to continue with their arbitration proceeding.

On August 12, 2003, Ecklund filed a Motion for Bankruptcy Rule 2004 Examination of Debtor. Due to a combination of circumstances not intended by the parties or the Court, the hearing on Ecklund's Rule 2004 motion was not held until January 26, 2004. Ecklund asserts that he originally filed the Rule 2004 motion because he became concerned that Debtor would frustrate his efforts to engage in discovery in the arbitration proceeding by taking the position that no discovery was allowable in that proceeding, or otherwise seeking a truncated discovery schedule, in an effort to deny Ecklund complete discovery. Since Ecklund filed his Rule 2004 motion, Ecklund and Debtor participated in a preliminary hearing with the arbitrators and the arbitrators allowed both parties the "opportunity to conduct fairly extensive discovery." Objection of Jay Ecklund to Petitioning

Creditor's Motion to Dismiss, ¶ 13 (Jan. 20, 2004). However, the arbitrating parties stipulated that it was not appropriate to resolve any fraudulent conveyance claim[1] in arbitration. Nevertheless, Ecklund still desires to examine Debtor with regard to the fraudulent conveyance claims. Thus, Ecklund has not abandoned his Rule 2004 motion.

Following Ecklund's motion, on December 22, 2003, M. H. Yacht filed a Motion to Dismiss Involuntary Petition With Consent of Debtor. Since M. H. Yacht filed the involuntary petition, it has remained the sole petitioning creditor as no other creditors have joined in the action. M. H. Yacht's motion stated in pertinent part that:

> 7. The settlement agreement does not contemplate or involve any consideration from, or transfer of property by, the Debtor.
>
> 8. The agreement provides for a conditional release by M. H. Yacht in favor of the Debtor.
>
> 9. The agreement for release of the Debtor by M. H. Yacht being conditioned upon performance by the Debtor's principal officer, M. H. Yacht seeks, with the consent of the Debtor, to dismiss its Involuntary Petition without prejudice against the refiling thereof in the event of a failure of performance of the obligations of the Debtor's principle officer under the terms of the settlement agreement.
>
> Petitioning Creditor's Motion to Dismiss (Dec. 22, 2003)

[1]Ecklund has asserted a fraudulent conveyance claim under O.C.G.A. § 18-2-74 in the arbitration proceeding. Debtor has opposed such claim on the grounds that it is not appropriate for resolution by the arbitration panel.

Ecklund filed an objection to the motion to dismiss on January 20, 2004, asserting three reasons: (1) Ecklund contends that he did not receive notice of the motion or the related order and notice as required by Federal Rule of Bankruptcy Procedure 2002(a)(4). Other creditors and interested parties listed on the bankruptcy matrix received such notice on January 2, 2004, and were ordered to notify the Court by January 20, 2004, of their request to be heard regarding the Motion to Dismiss. Order and Notice to Show Cause (Dec. 31, 2003). (2) The Motion to Dismiss should be denied or, at a minimum, postponed so that he can proceed with his Rule 2004 examination; and (3) Ecklund's final objection to the Motion to Dismiss is that it fails to adequately and fully set forth the substance of the agreement reached between Debtor and M. H. Yacht Sales, Inc and disclose other issues surrounding Debtor.

CONCLUSIONS OF LAW

Notice of Motion to Dismiss

Ecklund has cited lack of adequate notice as a reason for denying M.H Yacht's motion to dismiss. Ecklund was not listed on the certificate of service matrix and did not receive the Order And Notice to Show Cause Why Case Should Not be Dismissed. Likewise, the creditors receiving notice obtained a copy of the Order and Notice on January 2, 2004, but such notice only gave them until January 20, 2004, to notify the court of any objection. Such time frame is seemingly in conflict with Bankruptcy Rule 2002(a)(4) that

requires 20 days notice of "the hearing on the dismissal of [a Chapter 7] case." However, Ecklund has not indicated how he or the other creditors were prejudiced in any manner by the allegedly inadequate notice.

Bankruptcy Rule 9006(c)(1) provides that, subject to limited exceptions, "when an act is required or allowed to be done at or within a specified time by these rules or by a notice given thereunder or by order of court, the court for cause shown may in its discretion with or without motion or notice order the period reduced." Likewise 11 U.S.C. § 102(1)(A) provides that, "'after notice and a hearing' or a similar phrase-- means after such notice as is appropriate in the particular circumstances." Finally, a rule requiring notice and opportunity to object is adequately complied with if an objecting party receives actual notice and is afforded an opportunity to raise its objection. *See e.g.* In re GST Telecom, Inc., No. 00-1082, 2002 WL 1737445, at *7 (D. Del. Jul. 29, 2002); In re Glinz, 66 B.R. 88, 91 (D. N.D.1986) ("There is no showing that the attorney could have made any arguments with 20 days notice by mail that he could not have made with the actual notice he received at the hearing."). Ecklund's counsel argued Ecklund's position at the January 26, 2004, hearing and later submitted a brief to this Court outlining his position. In addition, no other creditor has come forward to object to the motion to dismiss since notice was sent on January 2, 2004. Because of these facts and because it is within my discretion to reduce the time for giving notice, I hold that there was no defect of notice in this situation.

Rule 2004 Examination

Ecklund's objection to the motion to dismiss is largely based on his desire to examine Debtor pursuant to Bankruptcy Rule 2004. Bankruptcy Rule 2004(a) states that, "[o]n motion of any party in interest, the court may order the examination of any entity." Examinations under Rule 2004 are allowed for the "purpose of discovering assets and unearthing frauds" and have been compared to a "fishing expedition." *See* In re Rafsky, 300 B.R. 152, 153 n. 2 (Bankr. D. Conn. 2003). Thus, the scope of a Rule 2004 examination is exceptionally broad. *See* In re Duratech Indus., Inc., 241 B.R. 283, 289 (E.D. N.Y. 1999). Rule 2004 is peculiar to bankruptcy law and procedure because it affords few of the procedural safeguards that an examination under Rule 26 of the Federal Rules of Civil Procedure does. *See* In re GHR Energy Corp., 33 B.R. 451, 454 (Bankr. D. Mass.1983).

In determining whether or not to order a Rule 2004 examination, the Rule requires that I balance the competing interests of the parties, weighing the relevance and necessity of the information sought by examination. *See* In re Coffee Cupboard, Inc., 128 B.R. 509, 514 (Bankr. E.D. N.Y. 1991) (limiting examination of corporate debtor's principal and scope of document production where information obtained could be utilized in unrelated state court proceeding); In re Drexel Burnham Lambert Group, Inc., 123 B.R. 702, 712 (Bankr. S.D. N.Y.1991) (holding movant entitled to production of documents). While the

information obtained through a Rule 2004 examination could be relevant to Debtor's bankruptcy case, the information is no longer necessary since M. H. Yacht and Debtor have reached an agreement and no other creditors have intervened to join in the involuntary petition.[2]

Ecklund's request for a Rule 2004 examination of Debtor came after it was granted relief from stay to settle its dispute with Debtor through arbitration. The popularity of arbitration rests in considerable part on its asserted efficiency and cost-effectiveness, characteristics said to be at odds with full-scale litigation in the courts. Further, I recently noted the strong federal policy favoring arbitration. Durango Georgia Converting, LLC v. TST Impreso, Inc.(In re Durango Georgia Paper Co.), No. 03-2049, slip op. at 9 (Bankr. S.D. Ga. January 22, 2004). Neither the Federal Arbitration Act nor the Uniform Arbitration Act mandate discovery in arbitration proceedings. *See* 21 Williston on Contracts § 57:90 (4th ed. 2003). Instead, the arbitrators control discovery. In fact, the arbitrators' authority over proceedings is so expansive that parties may not infringe upon the arbitrators' control over procedure; parties "may not superimpose rigorous procedural limitations on the very process designed to avoid such limitations." Forsythe International, S.A. v. Gibbs Oil Company Texas, 915 F.2d 1017, 1022 (5th Cir. 1990).

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[2] 11 U.S.C. § 303(b)(1) requires that any involuntary petition filed against a debtor with twelve or more creditors, as is the undisputed case here, must be commenced by "three or more entities, each of which is either a holder of a claim against such person that is not contingent as to liability or the subject of a bona fide dispute . . . " The three creditor requirement of § 303(b)(1) was never met in this case.

Notably, it was Ecklund that argued the dispute should be removed to arbitration. Ecklund stated that "[a]rbitration will not delay the administration of the case, but instead, it will enhance administration as this dispute is capable of efficient and expeditions resolution in arbitration." Motion of Jay Ecklund to Modify Automatic Stay, ¶20 (June 11, 2003). Further, Ecklund has conceded that discovery in the arbitration proceeding has been "fairly extensive." Objection of Jay Ecklund, ¶ 12. While Ecklund has stated that he, "is willing to narrow the scope of his Rule 2004 examination to the issue of avoidance actions,"[3] he has failed to explain how allowing expansive discovery under Rule 2004 effectuates the policy favoring arbitration and the efficient resolution of matters. Allowing information to be obtained through a Rule 2004 examination in this instance would undoubtedly impede the function of the arbitrators and detract from the efficient nature of the arbitration proceeding.

Also worth considering in this instance is the fact that Ecklund wishes to use the Rule 2004 examination to obtain information about a state law claim. [4] Because of this

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[3] *See* Brief in Support of Objection of Jay Ecklund, p.3 (Feb. 9, 2004)

[4] There is no dispute concerning the nature of Ecklund's claims as he has stated:

> The parties claims are traditional contract/state law claims and are clearly not core claims. They do not trace their genesis to the Bankruptcy Code, but are instead independent of the Bankruptcy Code.
>
> Motion of Jay Ecklund to Modify Automatic Stay, ¶18 (June 11, 2003)

fact, Ecklund still has an adequate remedy for relief if this Court denies his motion. After weighing the interests of the parties and the considerations discussed, I hold that Ecklund is not entitled to conduct a Rule 2004 examination of Debtor.

Disclosure of Agreement Between Petitioning Creditor and Debtor

11 U.S.C. § 303(j)(2) provides that an involuntary case may be dismissed on consent of all petitioners and the debtor and before entry of an order for relief, "only after notice to all creditors and a hearing . . . " The purpose of this section is "to avoid the filing of involuntary cases followed by collusive settlements between the petitioning creditors and the debtor . . . ." In re Rajneesh Neo-Sannyas Int'l Commune, 59 B.R. 49, 51 (Bankr. D. Or. 1986) (*quoting* 2 Collier on Bankruptcy, ¶ 303.37, pg. 303-117); *See also* In re Faberge Restaurant of Florida, Inc., 222 B.R. 385, 388 (Bankr. S.D. Fla. 1997) (holding involuntary Chapter 7 debtor's postpetition payment to one of creditors that had joined in filing involuntary petition did not render petition insufficient for lack of eligible creditors). Since the purpose of the Bankruptcy Code is to facilitate equal treatment to similar creditors, an involuntary petition cannot be dismissed solely upon the consent of the petitioners and the debtor unless the court finds that dismissal is in the best interest of all creditors. *See* In re Warren, 181 B.R. 136, 138 (Bankr. N.D. Ala. 1995) (holding proposed settlement did not treat similarly situated creditors equally and could not be approved); In re Wayne's Sport Haus, Ltd., 27 B.R. 521, 522 (Bankr. E.D. Mich. 1983) (refusing to grant unopposed motion

to dismiss where settlement provided that debtor's president would pay only petitioners).

Ecklund is not precluded from objecting to the motion to dismiss because his claim against Debtor is subject to a bona fide dispute. That is, a creditor can have standing to object to dismissal of an involuntary bankruptcy petition even though the creditor could not have joined in involuntary petition because its claim was subject to bona fide dispute. *See* In re Taub, 150 B.R. 96, 97-98 (Bankr. D. Conn. 1993) (holding that notice had to be given to all creditors, including nonpetitioning creditors, before case could be dismissed); In re Broshear, 122 B.R. 705, 707 (Bankr. S.D. Ohio 1991) (granting motion to vacate order dismissing involuntary Chapter 7 case unless petitioning creditors rescinded or repaid sums they received from debtor); Rajneesh, 59 B.R. at 51. Courts so holding have pointed to the fact that when Congress enacted the Bankruptcy Amendments and Federal Judgeship Act in 1984, it expressly eliminated the ability of a creditor with a claim subject to bona fide dispute to be a petitioning creditor. § 303(b)(1). Congress made no corresponding change in § 303(j) regarding which creditors must receive notice of the proposed dismissal. Since notice must be sent to all creditors, Congress must have intended that all creditors have standing to be heard on their objections to dismissal. Thus, the fact that there is a bona fide dispute between Debtor and Ecklund concerning any debt owed by Debtor does not preclude Ecklund from objecting to the motion to dismiss.

Ecklund has argued that the motion to dismiss is not in the best interest of the creditors. Specifically, he points to the fact that the motion fails to adequately and fully set forth the substance of the agreement between Debtor and the petitioning creditor, M. H. Yacht. The fact scenario in this situation is distinguishable from the majority of cases where courts have denied or closely scrutinized motions for relief where the debtor and petitioning creditor have reached a settlement because those cases (i.e., Faberge Restaurant, Warren, Wayne's Sport Haus) involved at least three creditors. Here, there was only one petitioning creditor. Even if no agreement had been reached and M. H. Yacht remained a petitioning creditor, there would have still been fewer than three creditors and dismissal would have been appropriate under § 303(b)(1).[5]

Despite the fact that there were never three petitioning creditors, granting the motion to dismiss in this instance without disclosure of the agreement reached between M. H. Yacht and Debtor could create the possibility in the future that a lone creditor could file an involuntary petition despite the three creditor requirement of § 303(b)(1) in an effort to "force the hand" of the debtor. Once in bankruptcy, the debtor might be more accommodating to settle its dispute with the petitioning creditor to the detriment of the other creditors. Such advantage gained by the petitioning creditor would be contrary to the spirit of the Bankruptcy Code that intends to put similarly placed creditors on equal footing. In

[5] *See* note 2, supra.

short, the sole petitioning creditor could improperly use this Bankruptcy Court as an unfair litigation tactic for settling two-party disputes. *See* In re Spade, 258 B.R. 221, 235 (Bankr. D. Colo. 2001) (holding that interests of creditors and alleged debtor were better served by dismissing involuntary Chapter 7 petition where it was little more than a two-party dispute).

While only minimal facts were disclosed regarding the agreement reached between M.H. Yacht and Debtor, I hold that such disclosure is sufficient to satisfy any concern about preferential accommodations being made to M. H. Yacht. The motion to dismiss states that Debtor has paid no consideration to M. H. Yacht. Instead, Debtor's principal has undertaken to perform Debtor's duty under a contract with M. H. Yacht. These representations, though skeletal, are affirmative representations of fact, relied upon by this Court. They provide clear evidence that Debtor has tendered nothing of value to M. H. Yacht. They also reveal that an insider has undertaken to perform the contract. This provides Ecklund a roadmap to follow if he chooses to seek relief in some other forum. As a bankruptcy matter, though, there is no basis for ordering any further disclosure of the agreement reached between M.H. Yacht and Debtor. Because there have been no further objections to M.H. Yacht's motion, dismissal of the involuntary petition is appropriate.

ORDER

Pursuant to the foregoing Findings of Fact and Conclusions of Law, IT IS

THE ORDER OF THIS COURT that Jay Ecklund's Motion for Bankruptcy Rule 2004 Examination of Debtor is DENIED.

IT IS FURTHER ORDERED that the Motion to Dismiss is granted.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia

This 24th day of March, 2004.

[redacted] Debtor - Sav'h Yacht Corp
Debtor's Atty. - Herne
Creditor - M H Yacht Sales
Creditor's Atty. Butler
[redacted] -James

R. Imperial
C. Rowe

3/30/04